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IN THE

Supreme Court of the United States

OCTOBER TERM, 1977

No. 76-1114

CALIFORNIA, *et al.*

Petitioners

v.

SOUTHLAND ROYALTY COMPANY, *et al.*

No. 76-1133

EL PASO NATURAL GAS COMPANY

Petitioner

v.

SOUTHLAND ROYALTY COMPANY, *et al.*

No. 76-1587

FEDERAL POWER COMMISSION

Petitioner

v.

SOUTHLAND ROYALTY COMPANY, *et al.*

ON WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR RESPONDENT CRANE COUNTY DEVELOPMENT COMPANY

Of Counsel:

F. M. PANNILL
PANNILL AND HOOPER
1100 Milam Building
Houston, Texas 77002

WILLIAM PANNILL
PANNILL AND HOOPER
1100 Milam Building
Houston, Texas 77002

Attorneys for Respondent Crane County Development Company

FIDELITY PRINTING COMPANY, HOUSTON

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OPINIONS BELOW

The opinion of the Court of Appeals is reported at 543 F.2d 1134 (Pet. App. 1a-11a)[1] and the relevant opinions

[1] This brief will follow the Federal Power Commission's system of referring to the appendix in the petition for certiorari as

and orders of the Federal Power Commission (Nos. 737 and 737-A) are reported at App. 598 and App. 708.

JURISDICTION

The judgment of the court of appeals was entered on December 13, 1976 (Pet. App. 12a-13a), and certiorari granted on June 27, 1977, in *California, et al.* v. *Southland Royalty Company, et al.*, No. 76-1114, *El Paso Natural Gas Company* v. *Southland Royalty Company, et al.*, No. 76-1133, and *Federal Power Commission* v. *Southland Royalty Company, et al.*, No. 76-1587. The cases have been consolidated (App. 746). Jurisdiction rests on 28 U.S.C. 1254(1) and Section 19(b) of the Natural Gas Act of 1938, 15 U.S.C. 717r(b).

QUESTION PRESENTED

Whether the reversionary interest existing under a fifty-year fixed-term oil and gas lease is rendered subject to Federal jurisdiction under the Natural Gas Act when the lessee makes an interstate sale of its interest in production.

STATEMENT

This case raises the question of FPC jurisdiction over two oil and gas properties in West Texas, the Waddell Lease in Crane County (App. 135) and the Goldsmith Lease in Ector County (App. 293). Both were subject to leases executed in 1925 that provided for a reversion of the property to the landowner after fifty years. The lessee, Gulf Oil Corporation, discovered oil and gas on both leases pursuant to its leasehold rights.

"Pet. App." and the appendix in this court as "App." Although the Federal Power Commission was succeeded by the Federal Energy Regulatory Commission on October 1, 1977, this brief continues to refer to the Federal Power Commission to avoid confusion.

1. Gulf's certificated interstate sales

In 1951, Gulf began sales of casinghead gas to El Paso Natural Gas Company from the Waddell Lease (App. 40). Gulf's sales were carried on in interstate commerce for resale to distributing companies on the El Paso pipeline system, which extends from Texas through New Mexico, Utah, Colorado, Arizona, and California (App. 119). As Seller, Gulf agreed to a customary "dedication" to the sales contract covering "all of Seller's surplus residue gas as herein defined" (App. 43). Gulf entered another contract with El Paso covering Waddell Lease sales in 1972 that included a "commitment" of "all volumes . . . from" those properties owned by Gulf Oil Corporation set forth on an exhibit to the sales contract (App. 87, 90-91). The 1972 contract adopted the 1951 contract by reference (App. 88). Although the record does not contain the exact terms of sales contracts to El Paso covering the Goldsmith Lease, the Federal Power Commission's brief states that "there are no material differences" between the leases (Br. 5 n.6).

Following this court's decision in *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672 (1954), Gulf applied to the FPC for a certificate of public convenience and necessity "with respect to the sale of natural gas" in interstate commerce to cover the Crane County sale (App. 2). The Commission held a public hearing on May 21, 1956, and promulgated its Findings and Order Issuing Certificates of Public Convenience and Necessity on May 28, 1956, noting that the applicants were "to render services as hereinafter described" (App. 26, 35). The Commission found that Gulf was "engaged in the sale of natural gas in interstate commerce for resale," and was therefore a "natural gas company within the meaning of the Natural Gas Act" and issued it a certificate (App. 36-37). Commissioner Digby concurred in the order, but stated that the Commission lacked power over

"the producing properties and gathering facilities of a natural-gas company", citing *inter alia FPC* v. *Panhandle Eastern Pipe Line Company*, 337 U.S. 498, 505.

2. Proceedings in the Texas courts

In the early 1970's, Gulf filed suit in the Texas courts to forestall expiration of the fifty-year term of the Waddell lease. The trial court denied Gulf's demand for additional lease time and held that the Waddell lease terminated by operation of law on July 14, 1975, exactly fifty years after its execution. The Court of Civil Appeals and the Supreme Court of Texas affirmed. *Gulf Oil Corporation* v. *Southland Royalty Company*, 496 S.W.2d 547, 548 (Tex. 1973) (App. 166, 168). The owners of the reversionary interest began seeking a market for gas sales attributable to their interest (App. 181-191).

On January 17, 1975, El Paso Natural Gas Company filed a Petition for a Declaratory Order by the Federal Power Commission to continue sales of the Waddell gas to the company after reversion of the property to the landowners (App. 117). On April 19, 1975, Texaco Inc. filed its petition covering the Goldsmith lease. On July 11, 1975, three days before reversion of the estate, the Commission issued Opinion 737 ordering both Gulf and the reversioners to continue deliveries to El Paso (App. 599). The Commission stated:

> In our opinion the various mineral reversioners may not sell gas from the two leaseholds in intrastate commerce without prior permission and approval of the Commission. Although we have discovered no case directly in point, we are of the opinion that the cases and the purpose of the Natural Gas Act inevitably lead to this view.

(App. 605). Motions for rehearing were filed and on September 3, 1975, the Commission issued Opinion 737-A, its order

on rehearing. The Commission reaffirmed the jurisdictional conclusion of Opinion 737 by stating:

> Upon the commencement of interstate sales under FPC certification, the sales became imbued with the public interest.

(App. 713).

3. Decision of the Court of Appeals

On petitions for review of the Commission's orders filed by the landowners,[2] the Fifth Circuit Court of Appeals reversed the Commission on December 13, 1976. 543 F.2d 1134. The court held that the FPC had no power over the gas owned by the reversioners because a lessee can only dedicate what he owns:

> The estates in the single tract are as separate as though they subsisted in separate parcels of land. Though it is unquestioned that Gulf's dedication covered all of the surplus residue gas it produced during its lease term, there likewise can be no question that, under well established concepts of property law, Gulf could not legally deal in or dedicate that portion of the gas which Southland might own upon termination of Gulf's estate.

543 F.2d at 1136-37. These petitions followed.

SUMMARY OF ARGUMENT

These cases arise from an attempt by the Federal Power Commission to assert abandonment jurisdiction over oil-and-gas leases expiring of their own terms. The landowners' conveyance, authoritatively interpreted under Texas law, lasted only fifty years, and more than half the term of the grant had expired when Gulf commenced sales of

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[2] Crane County Development Company moved to intervene in the case in the Court of Appeals "with full rights as a party." Crane County's motion was granted without opposition on March 8, 1976.

natural gas for resale in interstate commerce from the Waddell Ranch and thus rendered itself subject to FPC jurisdiction under the Natural Gas Act. Seeking to prolong gas deliveries from the property, El Paso Natural Gas Company persuaded the Federal Power Commission to direct that sales to El Paso had to continue even though the state courts had ousted the jurisdictional seller.

Such a result would run directly counter to settled interpretations by this Court of the Natural Gas Act and its sister statute, the Federal Power Act, in cases that rejected FPC jurisdiction over essentially local transactions. *FPC* v. *Panhandle Eastern Pipe Line Company*, 337 U.S. 498; *Connecticut Light & Power Company* v. *FPC*, 324 U.S. 515. The Commission chose to ignore these clear precedents and act on its own perception of the public interest. In doing so, it overreached its jurisdiction under the Natural Gas Act and was properly reversed by the Court of Appeals.

Constructions of the power of the Interstate Commerce Commission have no relevance to this problem, moreover, because the framers of the Natural Gas Act rejected that Act as a model.

ARGUMENT

PRIOR DECISIONS OF THIS COURT FORECLOSE THE FPC FROM ASSERTING JURISDICTION OVER THESE PROPERTIES UNDER THE NATURAL GAS ACT.

A. The Natural Gas Act does not reach local property interests such as these but only certain interstate sales and transportations of natural gas.

The Federal Power Commission, candidly admitting that it can find no clear legal precedent for its action, has attempted to exert its abandonment authority over property interests that are beyond FPC jurisdiction under the Natural Gas Act. The FPC's action is understandable: it seeks to capture every possible molecule of natural gas for the interstate market, which has been faced with growing shortages perhaps brought on by regulatory failures. *See FPC* v. *Texaco Inc.*, 417 U.S. 380, 400 and n.9. But the Court of Appeals was correct in reversing the Commission, because the FPC's orders here amounted to "an expansion of the Natural Gas Act to activities clearly not within its terms." *Mobil Oil Corp.* v. *FPC*, 463 F.2d 256 (D.C. Cir. 1971), *cert. denied*, 406 U.S. 976 (1972).

In these cases, the Commission exerted jurisdiction over the terms of ordinary expiring leases, granted by the landowners to a producer that rendered itself subject to the Natural Gas Act with interstate sales more than two decades after the conveyance. Thus the lease was far removed from any sale of gas in interstate commerce both in time and dispositive provisions. The FPC sought to augment the gas reserves of El Paso Natural Gas Company, but in directing the reversionary owners to produce their gas for the benefit of El Paso, the Commission arrived at an unprecedented result, forcing the reversionary owners into an assumption of Gulf's sale. Even though the reversion was prior in time and superior in law to Gulf's sales commitments, the Commission decided that Gulf's sales had resulted in a "dedication of gas reserves" to the interstate market. This is only a conclusory justification for the FPC's exercise of power.

In this Court, the Commission has dropped its argument that the reversionary interest was somehow "dedicated" to interstate commerce. There is clearly no dedication to be found anywhere in this record, as the Court of Appeals held. The FPC and the other petitioners have fallen back

instead on a novel theory amounting to the extension of Federal jurisdiction in rem over these local property interests. Thus, California argues that "[t]he Natural Gas Act imposes a regulatory requirement on the subject natual gas above local law and lease agreements" leading to a statutory "service requirement . . . which attache[s] to the gas" (Br. 8, 9). California is wrong.

Even if Congress has power to regulate these purely local interests in land, that power was not granted to the Federal Power Commission by the Natural Gas Act. The statutory service requirement urged by petitioners was rejected by this Court in *FPC* v. *Panhandle Eastern Pipe Line Company*, 337 U.S. 498 (1949), which held that ordinary lease transactions were among the matters left to the states by the Natural Gas Act.

In that case, as in this one, the Commission sought to extend its jurisdiction over gas reserves never dedicated to interstate commerce. The pipeline had conveyed leases in Kansas to an intrastate subsidiary. Although Panhandle Eastern had never made deliveries of gas from the leases and thus was neither selling nor transporting the gas in interstate commerce, the Commission sought to block the transfer. 337 U.S. at 501.

This Court held that the transaction fell within the jurisdictional exemptions of Section 1(b) of the Natural Gas Act, 15 U.S.C. 717(b), and was thus beyond FPC power. The Court construed the Natural Gas Act as not extending "federal regulation of the entire natural gas field to the limit of constitutional power," but as applying only to sales of natural gas in interstate commerce for resale, transportation of natural gas, and companies "engaged in" either a transportation or a sale, quoting *Panhandle Eastern Pipeline Company* v. *Public Service Commission of Indiana*,

332 U.S. 507, 516 (1947). The Court decided that Congress had purposely "left the transfer of gas leases to state regulation and outside the scope of the Commission's regulatory powers." 337 U.S. at 502.

The Panhandle Eastern case is a complete answer to the argument that the Natural Gas Act attaches to real estate in the form of oil and gas in place. Nor can there be any analytical difference between the transfer of a pipeline's undeveloped leases to an intrastate subsidiary and the transfer of a landowner's rights for a term of years. If anything, the landowner's distance from interstate commerce and thus FPC jurisdiction is greater. *Mobil Oil Corporation* v. *FPC*, 463 F.2d at 262-63.

Nor is *FPC* v. *Panhandle Eastern Pipe Line Company*, *supra*, an isolated precedent. In a series of natural-gas cases, cited by Commissioner Digby in his concurrence to the Gulf certificate order in this case (App. 39), this Court has held that the properties of a natural gas company such as Gulf were placed beyond FPC jurisdiction by Congress. Thus "the 'production or gathering' exemption applies to the physical activities, facilities, and properties used in the production and gathering of natural gas." *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672, 678, citing *Colorado Interstate Gas Co.* v. *FPC*, 324 U.S. 581, 598. Under the sister statute administered by the Commission, the Federal Power Act, this Court has held that Congress "meant what it said" when it limited the jurisdiction of the Commission to sales and transportations in interstate commerce and excluded local facilities. *Connecticut Light & Power Company* v. *FPC*, 324 U.S. 515, 530 (1945).

In all these cases, this Court has observed that Congress did not intend to bring under the Federal Power or Natural Gas Acts any transaction left to state jurisdiction under

Missouri v. *Kansas Gas Company*, 265 U.S. 298 (1924), and *Public Utilities Commission* v. *Attleboro Steam & Electric Company*, 273 U.S. 83 (1927). These cases held that sales and deliveries "essentially national in character" were beyond the reach of state regulation. *See Missouri* v. *Kansas Gas Co.*, 265 U.S. at 308. But activities essentially local could be regulated by the states. *Id.* at 309. It is difficult to imagine any transaction more essentially local than the conveyance of real property; and indeed this Court has observed that regulation of real property rights in oil and gas is "essentially local" in character. *Ohio Oil Company* v. *Indiana*, 177 U.S. 190, 211-212 (1900). *See FPC* v. *Southern California Edison Co.*, 376 U.S. 205, 211-14 (1964); *Mobil Oil Corp.* v. *FPC*, 463 F.2d at 262-63; *Duke Power Co.* v. *FPC*, 401 F.2d 930, 938-40 (D.C. Cir. 1968).

This "bright line easily ascertained" simply forecloses the argument that the Natural Gas Act gives the Commission the power to compel property owners to carry on a "sale" or to render a "service" they never agreed to. *FPC* v. *Southern California Edison Company*, 376 U.S. at 215. "The FPC is limited by the provision establishing its jurisdiction, and we do not find in that provision, rooted as it is in a sale in interstate commerce, any basis for reaching out to cover the landowner's lease . . . ." *Mobil Oil Corp.* v. *FPC, supra*, 463 F.2d at 263. Petitioners rely heavily on dicta about "service" from other cases to support their claim that this Texas property is now jurisdictional in itself. Yet every one of these cases involved a natural gas company making a sale of natural gas in interstate commerce for resale clearly subject to FPC jurisdiction. "[T]his Court does not decide important questions of law by cursory dicta inserted in unrelated cases." *Permian Basin Area Rate Cases*, 390 U.S. 747, 775 (1968).

Nor does the *Rayne Field* case broaden the Commission's jurisdiction to include these property interests. That jurisdictional holding was also "rooted . . . in a sale in interstate commerce" of natural gas for resale. *Mobil Oil Corporation* v. *FPC*, 463 F.2d at 263. There producers like Gulf in this case withdrew from sales contracts after an adverse decision and sold gas in place under "lease-sale agreements," with payments geared to production. All minerals were reserved to the sellers except natural gas, which was sold to the pipeline. *United Gas Improvement Co.* v. *Continental Oil Co.*, 381 U.S. 392, 395-96 (1965). This Court correctly discerned that whatever the form of the transaction, the substance of it was a sale for resale in interstate commerce. The Court will find no such interstate sale of natural gas in the conveyance in 1925 in this case from the landowners to Gulf. The Waddells did not even receive a royalty based on price, but only ⅛ of 4 cents for each Mcf of casinghead gas produced (App. 137).

Thus by the weight of authority these "conventional" leases are outside the scope of FPC jurisdiction under the Natural Gas Act. Since Gulf obviously lacked power to dedicate the landowner's reversionary interest to interstate commerce, the Court of Appeals' decision is correct and should be affirmed.

B. The Interstate Commerce Act offers no aid in the construction of the Natural Gas Act.

The Commission urges the Court to construe the abandonment provision of the Natural Gas Act the way it claims the Interstate Commerce Act has been construed (Br. 21-29; see El Paso Br. 17-21; AGD Amicus Br. 6-7). But Section 7(b) has already been construed to the contrary in *FPC* v. *Panhandle Eastern Pipe Line Company*, 337 U.S. at 508-09.

And even if the question were open, the legislative history denies the Commission any power over lessors similar to that claimed on brief for the Interstate Commerce Commission. This Court quoted Senator Connally of Texas in an exchange in the Senate debates on the Natural Gas Act with Chairman Wheeler of the Interstate Commerce Committee:

> "Mr. CONNALLY. Is it not also true, even though the utility commissioners advocate it, that whenever a Federal agency takes over an activity such as this the State authorities begin to shift or lose their responsibility? If we turn this over to the Interstate Commerce Commission, essentially what they do will be reflected all over the country, because the interstate rates will be superimposed on the State commissions and they must necessarily be governed by them. Did not that happen to the railroads?
>
> "Mr. WHEELER. There is no doubt about that, but this is an entirely different situation.
>
> "Mr. CONNALLY. Yes; one involves the railroads and the other involves gas.
>
> "Mr. WHEELER. No. There is no attempt and can be no attempt under the provisions of the bill to regulate anything in the field except where it is not regulated at the present time. It applies only as to interstate commerce and only to the wholesale price of gas." 81 Cong. Rec. 9313.
>
> "Mr. AUSTIN. Then, it would leave to the future the right to meet any effort on the part of the central government to acquire the natural resources of the State of Montana, or the State of Vermont, or any other State?
>
> "Mr. WHEELER. Oh, yes. It does not touch it in any way, shape, or form, except to require the furnishing of information.

> "Mr. AUSTIN. I have great fear of these occult methods of acquiring the natural resources of our several States." 81 Cong. Rec. 9314.

Quoted in FPC v. *Panhandle Eastern Pipe Line Company,* 337 U.S. at 511-12 n.15. Based on this case, this Court has contrasted the expansive powers of the I.C.C. to regulate exempt operations with the "specific grounding" of limited FPC jurisdiction under the Natural Gas Act. *American Trucking Associations* v. *United States,* 344 U.S. 298, 313 (1953). It is plain that the Natural Gas Act cannot be construed by reference to any powers of the Interstate Commerce Commission.

Conclusion

The Natural Gas Act provides clearly that its provisions "shall not apply" to activities under State control before the passage of the statute. These activities include local property interests and their transfer. As Mr. Justice Jackson stated in *Connecticut Power & Light Co.* v. *FPC*, 324 U.S. at 528-529,

> It is hard for us to believe that Congress meant us to read "shall have jurisdiction" where it had carefully written "but shall not have jurisdiction." . . . [I]t is the provision which loomed importantly in the mind and speech of its sponsors, perhaps was necessary to get the bill passed, and is one which the Commission must observe and the courts must enforce.

Limits on the jurisdiction of the FPC may cut against the interests of El Paso Natural Gas Company and the State of California. But this Court has consistently declined to overturn such congressional assumptions embedded in the framework of the Act. *FPC* v. *Texaco Inc.*, 417 U.S. 380, 400 (1974). This Court should affirm the decision of the Court of Appeals.

Respectfully submitted,

WILLIAM PANNILL,
Attorney for Respondent Crane County Development Company

Of Counsel:

F. H. PANNILL,
Pannill and Hooper
1100 Milam Building
Houston, Texas 77002

October, 1977

CERTIFICATE OF SERVICE

I hereby certify that on this 24th day of October, 1977, three copies of the foregoing Brief for Respondent were mailed, postage prepaid, to counsel for all parties of record.

WILLIAM PANNILL
Counsel for Respondent
Crane County Development Company